



# STATUTORY REPORT ON CORPORATE GOVERNANCE 2010

This statutory report on corporate governance cf. section 107(b) of the Danish Financial Statements Act, forms part of Management's Review in the 2010 annual report covering the financial period 1 January - 31 December 2010.

The statement is divided into three sections:

- Corporate Governance
- A description of Topsil Management
- An account of the main elements in the internal control systems and risk management in connection with financial reporting.

## CORPORATE GOVERNANCE

Pursuant to s. 107(b) of the Danish Financial Statements Act and clause 4.3 of the "Rules for issuers of Shares – NASDAQ OMX Copenhagen", listed companies must report on how they address the recommendations published by The Committee on Corporate Governance in Denmark on 1 April 2010.

In this report on corporate governance, companies must apply the "comply or explain" principle according to which they must either comply with the recommendations or explain why the recommendations are not complied with in full or in part. The purpose is to create transparency in respect of a company's management structure and it is up to the individual companies to assess whether it is prudent to comply with the recommendations.

Topsil's statutory report on corporate governance, including a consideration of each item under the recommendations, can be found on the Company's website at

[www.topsil.com/files/pdf/UKcorporategovernance2010.pdf](http://www.topsil.com/files/pdf/UKcorporategovernance2010.pdf)

## TOPSIL MANAGEMENT

Topsil's management comprises the Board of Directors and the Management Board.

### The board of directors

The Board of Directors has the overall responsibility for the management of the Group and supervises the Management Board. The Board of Directors lays down the policies for the Company's business strategy, organisation, accounting and financing and appoints a Management Board to be in charge of the day-to-day operations of the Group.

The Board of Directors is made up of four members elected by the shareholders and two members elected by the employees. See page 32-34 of the 2010 annual report for an overview of the Board of Directors and the Management Board.

Pursuant to the Articles of Association, the members of the Board of Directors elected by the shareholders are elected for terms of one year at the annual general meeting. The term for the current Board of Directors expires on 14 April 2011 and the members are eligible for re-election. According to the rules of procedure for the Board of Directors, the retirement age for Board members is 70 years.

The term of Board members elected by the employees is four years as laid down by the Danish Companies Act. Members elected by the employees have the same rights, duties and responsibilities and they receive the same fees as the other members of the Board of Directors. The term of the current members elected by the employees expires in 2011 and employee elections will be held on 5 April 2011. Further details on the rules for election of employee representatives can be found on the Company's website under "Management".

When composing the Board of Directors, the aim is for the majority of the Board members elected by the shareholders to be independent of special interests relative to the Group, major shareholders, chief suppliers and key accounts.

Three of the four Board members elected by the shareholders are independent of special interests. Topsil's Deputy Chairman, Eivind Dam Jensen, is not independent, as he controls 12.2% of the capital in Topsil and owns and leases the property at Linderupvej 4, Frederikssund, to Topsil. The transactions are disclosed in a separate note to the financial statements.

Employee representatives are not considered to be independent due to their employment relationship with Topsil.

The Board of Directors is composed of members who represent general management experience in globally oriented industrial businesses, have industry insight and possess professional skills pertaining to listed companies' financial and economic matters.

Board meetings are held at least six times a year. The Board of Directors follows an annual schedule fixed each year in November together with the financial calendar and otherwise convenes as and when deemed necessary. One of the meetings is held at the subsidiary Cemat Silicon S.A. in Warsaw. In 2010, five ordinary and four extraordinary Board meetings were held together with a strategy seminar determining the most important tasks in relation to the overall strategic management.

The Board of Directors conducts its business in accordance with the rules of procedure, which comply with the provisions of s. 130 of the Danish Companies Act applicable to listed companies. Among other things, the rules of procedure contain guidelines for the division of responsibilities between the Board of Directors

and the Management Board, and provide for the application of minute books, a register of shareholders and other protocols. The rules of procedure determine the Board of Directors' duties to actively discuss the Company's organisation and internal control procedures as well as its duties to actively follow up on plans, budgets and the cash position, as well as other important issues.

### **Evaluation of the board of directors and management board**

The evaluation of the working methods, skills, efforts, interaction and performance of the Board of Directors and Management Board forms part of the annual schedule for the Board of Directors and is included as an item on the agenda of the annual general meeting.

The Chairman is in charge of the evaluation on the basis of a working document filled in by each Board member. The individual items are discussed openly among the members of the Board of Directors and the Management Board and the conclusions are recorded in the minute book. The self-evaluation is considered to be a tool for mapping the strengths and weaknesses of the management. It is also used as the recruitment base for new Board members and selection of future focus areas for the Board work. In 2010, the self-evaluation did not give rise to any significant changes in focus areas or the composition of the Board of Directors.

### **Board committees**

As the only committee under the Board of Directors Topsil set up an Audit Committee in 2009. Tasks relating to nomination and remuneration are considered to be of a scope that can be handled by the chairmanship. The latter is regulated by the Company's remuneration policy.

## Audit committee

The Audit Committee monitors the Group's financial reporting, accounting policies, internal control procedures and the framework for the independent auditors. Topsil's Audit Committee held six meetings in 2010.

As from April 2010 the Committee consists of Michael Hedegaard Lyng, chairman, and Jørgen Frost, deputy chairman. The Audit Committee members are elected by the Board of Directors from among its members and in compliance with Danish law, at least one of the two members must be an accounting expert. The Committee conducts annual self-evaluation to assess each member's performance.

The Audit Committee has worked out its terms of reference and a detailed annual schedule. According to the terms of reference, the tasks of the Audit Committee include approval of relevant guidelines and policies and discussions of material accounting policies applied by the Group. Furthermore, the Committee is currently considering whether individual controls should be extended and tightened to ensure compliance and improvement of the internal control procedures in the Group companies.

Further details on the Audit Committee's terms of reference can be found on the Company's website.

## Management board

Topsil's Management Board comprises two registered executive officers, the CEO and the EVP, Logistics, Sales & Marketing. The CEO is responsible for the day-to-day management of the Company in accordance with the guidelines laid down by the Board of Directors. Also, the Management Board is responsible for submitting proposals for the Group's overall strategies,

action plans, objectives and operating and investment budgets to the Board of Directors.

## Remuneration policy

Topsil's remuneration policy for the Board of Directors and the registered executive officers reflects the shareholders' and the Company's interests and must support the long-term objectives. Furthermore, the Company seeks a compensation package for the Board of Directors and the Management Board which is consistent with market levels to retain the current management and attract new qualified candidates.

The remuneration policy can be found on the website and will be presented to the shareholders for approval at the annual general meeting to be held on 14 April 2011.

## Remuneration of the board of directors

For the financial year 2010, the members of the Board of Directors of Topsil received a fixed annual remuneration of DKK 150,000. The Chairman received double remuneration and the Deputy Chairman one and a half times the basic remuneration for their extended Board tasks. The members of the Audit Committee received DKK 37,500 and the chairman received double that amount. Total remuneration to the Board of Directors came to DKK 1.2 million, as specified in note 5.

The Board of Directors receives no options, bonus or any other performance-related pay and is not covered by Topsil's pension scheme.

## Remuneration to the management board

The Board of Directors believes that a combination of fixed and performance-based compensation to the Management Board helps the Company to attract and retain the best

qualified executive officers while at the same time encouraging long-term value creation for the shareholders. Performance-related incentive schemes contribute to promoting behaviour that supports the achievement of the Company's long-term objectives. Against this background, the Board of Directors resolved to introduce incentive remuneration to the Management Board and other managerial employees of the Group.

The Management Board's compensation package comprises four elements: a fixed basic salary including company car, telephone, etc., a bonus based on the financial results achieved, pensions and a share option scheme.

The bonus scheme for the CEO comprises a bonus of 1% of profit before tax and 4% of the increase in the profit before tax relative to the previous year. For the EVP, Logistics Sales & Marketing, the corresponding rates are 0.7% and 2.8%, respectively.

Topsil's Management Board and a number of managerial employees have been granted warrants. The Management Board's share of these warrants, the terms and conditions and their valuation are disclosed in note 6 to the financial statements. Topsil's current incentive-based remuneration scheme and guidelines have been approved by the shareholders and are available on Topsil's website under 'Investor Relations'. Some of the criteria of the option scheme do not comply with the recommendations of the Committee on Corporate Governance in Denmark issued on 1 April 2010 and the scheme will be reconsidered in 2012 when it expires.

In 2010, the total remuneration to the Management Board came to DKK 7.2 million as specified in note 4. Topsil did not provide any substantial or atypical contributions to non-pay

benefits, severance plans, etc. to the Management Board in 2010.

### **Material agreements with management**

Other than as provided above, the Group has not entered into any material agreements with the Management.

The members of the Management Board are employed under executive service contracts. The service contract for the CEO is terminable by the CEO giving a notice of nine months. Termination by the Company is subject to 18 months' notice. In the event of a change of control of the Company (more than 50% of the shares or the voting rights) to a legal entity or a person, the notice given by the CEO will be extended to 12 months and the notice given by the Company will be extended to 24 months. The CEO is subject to a non-competition clause.

The service contract for the EVP, Logistics, Sales & Marketing is terminable by the EVP giving six months' notice, whereas termination by the Company is subject to 12 months' notice.

## **INTERNAL CONTROL SYSTEMS AND RISK MANAGEMENT RELATING TO THE PRESENTATION OF ACCOUNTS**

The Board of Directors of Topsil has the overall responsibility for the establishment of an efficient risk management system, comprising systematic internal controls and follow-up. Risk management and internal controls in relation to the financial reporting process are monitored by the Audit Committee.

### **General risk assessment and management**

As part of the Board of Director's annual strategy review, management conducts an overall risk assessment for the Group in order to determine which processes and factors, internal as well as external, could possibly affect the Group's business platform and development.

The risk assessment mainly comprises identification of business risks and control measures are identified for the most significant risks, e.g. in the form of action plans to reduce and handle risks.

### **Risk assessment and internal control systems at Topsil**

In connection with the current follow-up on the Group's strategy and development, Management assesses the identified risks and considers any new risks during the strategy period.

The objective of risk management is not to eliminate all risks, but to actively determine which risks are acceptable to and manageable by the Group and which risks to avoid entirely. Risk management is an integral part of the day-to-day business management and is subject to continuous review by Management. Management believes that the most significant

risks, in addition to financial risks, relate to supplier and customer relations due to the limited number of suppliers who can supply raw materials of a sufficient quality and customers demanding the Group's finished goods.

The Group has chosen to arrange for insurance cover within a number of general areas, including all risks insurance (machinery, equipment, inventories and business interruption), transport insurance, professional and product liability insurance, debtor insurance and directors' and officers' liability insurance. In addition, the Group has taken out workers' compensation insurance based on local conditions.

The Group operates with a low-risk profile and for this reason currency, interest rate and credit risks arise only in connection with commercial relations. It is the Group's policy not to actively speculate in financial risks.

Due to the nature of its operations and financing, the Group is exposed to fluctuations in exchange rates and interest rates. The Group manages its financial risks by means of a model to manage its cash forecasting.

The Group's currency, interest rate, credit and liquidity risks are described in a note to the consolidated financial statements.

### **Risk assessment relating to the financial reporting process**

The overall risk assessment also comprises risks relating to financial reporting and hence matters which could affect the completeness, accuracy and valuation-related matters relative to the Group's financial reporting. The risk assessment also comprises the risk of loss or misuse of assets.

## Control system

Topsil's CEO is responsible for maintaining efficient internal controls. The CEO has organised the staff functions in a Management Team. The Management Team comprises the CEO and seven managers and specialists, who are each responsible for the internal control of their respective areas of responsibility, such as sales, logistics, procurement, production, quality assurance, finance and IT. A description of the management structure at Topsil can be found on the Company's website.

All subsidiaries and business units of the Group have appropriate internal controls, covering the most significant risks. Internal policies and procedures, manuals and legislation and any other external regulation form the basis of the internal control environment, and the Group's employees are held responsible through organisational structures in the Group with clearly defined responsibilities and authority. The Group finance function performs current controlling activities in the subsidiaries and the results are reported to Management.

Control measures may alleviate the identified risks and ensure compliance with the basic criteria for financial reporting. The Group's control measures comprise general as well as detailed controls to prevent, identify and correct errors and irregularities. The Group has the following overall control measures:

- Manual controls — examples of important manual controls are signed bookkeeping lists, reconciliations, rights of access, master data and segregated functions to the extent permitted by the size of the organisation
- Programmed controls – examples of important programmed controls are

validation of entries, including that data is registered and applied centrally, automatic reconciliation of invoices with purchase orders and other reconciliation between the ERP modules

- General IT control – examples of important IT controls are user administration, production and test environment and backup procedures

Documentation of procedures is part of the internal control system and consists of flowcharts of procedures and descriptions of control measures. The process comprises formal as well as informal procedures used by Management, process owners and control operators, including assessments of results relative to budgets, strategy plans and selected key performance indicators (KPIs). The Group has established procedures to provide Management with a basis for assessing the Group's financial position. These procedures/reports comprise i.a.:

A review of strategic and business objectives at least every second year

Formalised annual budget, forecast and estimation procedures

Furthermore, the following is reported to Management on a current basis:

- Financial results and financial position, including analysis of cash flows and financial structure in the parent company and subsidiaries
- Comparison of budgeted financial results, results from previous years and actual results
- Project management and cost control as well as current project reporting, follow-

up and review of accounting policies and estimates

Also, the external auditors report to Management and the Audit Committee who assess the results of current investigations prepared to determine to what extent Management and the Audit Committee can rely on the reports/processes which are primarily prepared and performed by the finance department.